Nos. 15-233 & 15-255

IN THE

Supreme Court of the United States

THE COMMONWEALTH OF PUERTO RICO, ET AL.,
Petitioners,

v.

FRANKLIN CALIFORNIA TAX-FREE TRUST, ET AL.,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the First Circuit

BRIEF FOR *AMICUS CURIAE* SCOTIABANK DE PUERTO RICO, AS AGENT FOR LOCAL BANK LENDERS TO PREPA, IN SUPPORT OF RESPONDENTS

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INTRODUCTION AND INTEREST OF *AMICUS CURIAE*[1]

Scotiabank de Puerto Rico serves as agent for a group of Puerto Rico-based banks that has extended approximately $550 million in credit to PREPA, the Puerto Rico Electric Power Authority. These local banks include Scotiabank de Puerto Rico, Oriental Bank and Firstbank Puerto Rico. PREPA used the line of credit provided by these local banks to purchase the fuel oil needed to generate electricity for Puerto Rico. As a result, that line of credit is known as the "fuel line."

The local banks have a significant interest in the outcome of this appeal. The Puerto Rico Public Corporation Debt Enforcement and Recovery Act, if upheld, would fundamentally alter the contractual arrangement between PREPA and its creditors, including the local banks. When the local banks agreed to extend credit to finance PREPA's operations, they assumed the risk that *Congress* could potentially enact bankruptcy legislation that would apply to PREPA. But they never contemplated that *Puerto Rico* would be able to enact its own bankruptcy statute, let alone a statute that is significantly less protective of the rights of creditors than the federal Bankruptcy Code.

The Recovery Act not only conflicts with the contractual arrangement between PREPA and the

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[1] No counsel for a party authored this brief in whole or in part, and no person other than *amicus* Scotiabank de Puerto Rico, Oriental Bank and Firstbank Puerto Rico contributed money to fund the preparation or submission of this brief. All parties to this case have filed letters granting blanket consent to the filing of *amicus curiae* briefs.

local banks; it is also unnecessary to PREPA's ongoing effort to address its financial problems. For over a year, PREPA and its creditors, including the local banks, have worked tirelessly to negotiate a *consensual* restructuring of PREPA's debt. The result was a major step forward: In November 2015, PREPA and most of its creditors entered into a restructuring support agreement, or RSA, which will relieve PREPA of significant financial burdens and require the utility to reform and modernize its operations. The RSA—achieved outside the context of any bankruptcy proceeding, and well *after* the district court struck down the Recovery Act—refutes any assertion that the Recovery Act is needed to facilitate negotiations between PREPA and its creditors.

But the local banks' interest in this case goes further. As financial institutions based in Puerto Rico, the banks in the fuel line syndicate play a vital role in the island's economy. The local banks thus support the Commonwealth's plans and initiatives to address the island's fiscal problems in a manner that both protects the people of Puerto Rico and fosters an environment for investment and economic growth.

The Recovery Act, however, is not the way to achieve the Commonwealth's objectives. Future investors will recoil at the prospect that Puerto Rico might at any time enact new legislation to allow municipalities to shed their debts. The Recovery Act, moreover, is so unfavorable to creditors—and so much less protective of creditors' rights than the federal Bankruptcy Code—that it will inevitably affect the financing available to Puerto Rico. Reinstatement of the Recovery Act would thus hurt rather than help Puerto Rico as it seeks to regain the confidence of investors and spur the economic growth that it urgently needs.

BACKGROUND

The Commonwealth of Puerto Rico and its corporations and municipalities owe approximately $72 billion in public debt. PREPA in particular owes over $9 billion to its creditors.[2]

Founded in 1941, PREPA has broad authority to "determine, fix, alter, change and collect reasonable rates, fees, rentals, and other charges for the use of installations of the Authority, or for electric power services."[3] Until 2014, however, PREPA did not have independent regulatory oversight, and its operations suffered as a result. PREPA's power plants are outdated and experience frequent power failures.[4] PREPA's payroll is significantly larger than the average utility payroll on the mainland.[5] In addition, PREPA failed to collect approximately $1 billion in

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[2] Michael Corkery & Mary Williams Walsh, *Puerto Rico's Governor Says Island's Debts Are 'Not Payable'*, N.Y. TIMES (June 28, 2015), http://www.nytimes.com/2015/06/29/business/dealbook/puerto-ricos-governor-says-islands-debts-are-not-pay able.html.

[3] P.R. Electric Power Authority Act, P.R. LAWS ANN. tit. 22 § 196(l) (1941).

[4] *See* Steven Mufson, *Is It Lights Out for Puerto Rico?*, WASH. POST. (July 25, 2015), https://www.washingtonpost.com/business/economy/is-it-lights-out-for-puerto-rico/2015/07/24/61c6e51c-29a 7-11e5-a250-42bd812efc09_story.html; Anne O. Krueger et al., *Puerto Rico – A Way Forward*, 8, 18 (June 29, 2015), http://www.bgfpr.com/documents/puertoricoawayforward.pdf [hereinafter, the "Krueger Report"]; Hearing Memorandum, H. Subcomm. on Energy and Mineral Res., *Exploring Energy Challenges and Opportunities Facing Puerto Rico* 2-4 (Jan. 11, 2016), http://docs.house.gov/meetings/II/II06/20160112/104355/ HHRG-114-II06-20160112-SD002.pdf.

[5] Mufson, *supra* note 4.

past-due receivables from customers, including government entities,[6] and for years it also failed to require various of Puerto Rico's municipalities to pay in full for their electricity.[7]

The fuel line for which Scotiabank de Puerto Rico serves as agent dates back to a Credit Agreement entered on May 4, 2012. The purpose of the fuel line was to finance PREPA's fuel oil purchases, which are classified as "Current Expenses of the System" under the Trust Agreement governing PREPA's bond debt.[8] In the Trust Agreement, PREPA covenanted that it would pay all "Current Expenses" on a priority basis, before other obligations, and that it would "at all times fix, charge and collect reasonable rates and charges" to pay such Current Expenses.[9] The Credit Agreement further provides that PREPA's obligations on the fuel line—like the fuel oil purchases financed by the fuel line—are to be treated as "Current Expenses" under the Trust Agreement, meaning that PREPA would be required to raise its rates if necessary to pay those obligations.[10]

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[6] FTI Capital Advisors, *Accounts Receivable and CILT Report*, 9 (PREPA Presentation, Nov. 15, 2014), *available at* http://www.aeepr.com/Docs/restructuracion/PREPA%20AR%20 and%20CILT%20Report%20Final.pdf.

[7] Mary Williams Walsh, *How Free Electricity Helped Dig $9 Billion Hole in Puerto Rico*, N.Y. TIMES (Feb. 1, 2016), http://www.nytimes.com/2016/02/02/business/dealbook/puerto-rico-power-authoritys-debt-is-rooted-in-free-electricity.html?ref=dealbook&_r=0.

[8] Credit Agreement § 2.14.

[9] Trust Agreement §§ 502, 505.

[10] Credit Agreement §§ 5.09, 2.14; Trust Agreement §§ 502, 505.

PREPA, however, has never adjusted its rates to ensure that it could meet its obligations under the Credit Agreement. Indeed, *since 1989*, PREPA has not raised the "base rate" that it charges customers to cover debt service and expenses besides fuel[11]—even though it is required to do so not only by its loan agreements but also under Puerto Rico law.[12] The "base rate" charged to customers has instead remained constant, even as the overall rates paid by customers have decreased significantly due to the recent decline in oil prices.[13]

On June 28, 2014, Puerto Rico enacted the Puerto Rico Public Corporation Debt Enforcement and Recovery Act, or the "Recovery Act."[14] Within three days, on July 1, 2014, rating agencies downgraded

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[11] Robert Slavin, *Puerto Rico Energy Commission Rejects Insurer's Rate Increase Petition*, BOND BUYER (Oct. 1, 2015), http://www.bondbuyer.com/news/regionalnews/puerto-rico-energy-commission-rejects-insurers-rate-increase-petition-1085893-1.html.

[12] *See* 2014 P.R. Laws Act No. 57, § 2.8 (establishing an energy commission that "shall guarantee that the approved rate will be sufficient to: (i) guarantee payment of principal of and interest on bonds and other financial obligations of PREPA; and (ii) comply with the terms and provisions of the agreements entered into with or in benefit of buyers or holders of any bonds or other financial obligations of PREPA").

[13] *Compare* P.R. Elec. Power Auth., Monthly Reports to the Governing Board June 2014, at 5 (2014) (average overall rate approximately 26 cents per kilowatt-hour), *available at* http://tinyurl.com/jf7u9do, with P.R. Elec. Power Auth., Monthly Reports to the Governing Board December 2015, at 5 (2015) (average overall rate approximately 19 cents per kilowatt-hour), *available at* http://tinyurl.com/jf7u9do.

[14] 2014 P.R. Laws Act No. 71.

PREPA's bonds,[15] which triggered an event of default under the Credit Agreement. The local banks, seeking to cooperate with PREPA and the Commonwealth, promptly entered into the first of many forbearance agreements with PREPA.

Although PREPA asserts in its amicus brief that the Recovery Act spurred negotiations on a consensual restructuring (PREPA Br. at 11), the opposite is true. The Recovery Act reduced PREPA's incentive to negotiate, and little progress was made before the district court struck down the Act on February 6, 2015. Only after that decision—on June 1, 2015—did PREPA deliver a proposed recovery plan to creditors, as required by its forbearance agreements. And only then could PREPA and its creditors begin to negotiate in earnest on a consensual restructuring.

In early November 2015—after intense negotiations—PREPA, most of its bondholders, and the local banks entered into the RSA, the restructuring support agreement. The RSA provides for a comprehensive restructuring of PREPA's debt. According to PREPA's Chief Restructuring Officer, Lisa Donahue, the terms of the RSA are "fair" and "equitable," and she could not say that PREPA would have received a "better economic deal" in a case under Chapter 9 of the Bankruptcy Code.[16]

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[15] *See* Robert Slavin, *PREPA Downgraded as Payment Comes Due*, BOND BUYER (July 1, 2014), http://www.bondbuyer.com/news/regionalnews/prepa-downgraded-as-payment-comes-due-1064038-1.html.

[16] *See Exploring Energy Challenges and Opportunities Facing Puerto Rico: Oversight Hearing Before H. Comm. on Nat. Res., Subcomm. on Energy and Mineral Res.*, 114th Cong. (Jan. 12, 2016) (testimony of Lisa Donahue at 1:06:00-1:08:32), *available*

In connection with negotiations on the RSA, PREPA proposed to invest approximately $2.3 billion in new infrastructure to convert existing plants to natural gas and improve the efficiency of its plants.[17] PREPA also proposed to cut costs by approximately $320 million per year.[18] Consistent with those proposals, the RSA itself includes detailed agreements regarding operational improvements, PREPA's future rate structure and new capital investment.[19]

Consummation of the RSA is contingent upon several milestones, including enactment of implementing legislation by the Commonwealth. On February 16, 2016, Governor Alejandro Garcia Padilla signed legislation designed to implement the RSA after it was approved by the Puerto Rico Senate and House of Representatives.[20]

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at http://naturalresources.house.gov/calendar/eventsingle.aspx?EventID=399769.

[17] *See* PREPA Public Disclosure, PREPA's Transformation: A Path to Sustainability, Annex A (July 22, 2015), *available at* http://emma. msrb.org/ER906457-ER708173-ER1109700.pdf.

[18] *Id.*

[19] *See* PREPA Public Disclosure, Restructuring Support Agreement, Schedule V (Nov. 5, 2015), *available at* http://emma. msrb.org /EP884716-EP684716-EP1086412.pdf.

[20] Alex Lopez, *Puerto Rico Approves Electric Utility Restructuring Bill*, BLOOMBERG BUSINESS (Feb. 17, 2016), http://www.bloomberg.com/news/articles/2016-02-17/puerto-rico-senate-recesses-without-utility-debt-restructuring.

ARGUMENT

I. ENFORCEMENT OF THE BANKRUPTCY CODE'S PLAIN PREEMPTIVE LANGUAGE IS ESSENTIAL TO PROTECT THE LEGITIMATE EXPECTATIONS OF PREPA'S LENDERS.

In its amicus brief to this Court, PREPA proclaims that there was a "common understanding" among its creditors that "the Commonwealth could enact a restructuring law" if PREPA faced difficulty meeting its obligations. PREPA Br. at 2, 18-19. This is entirely baseless. PREPA accessed the credit markets on the understanding that—absent Congressional action—it would *not* be eligible to commence a proceeding to compel creditors to adjust their claims. The Recovery Act represents a *post hoc* repudiation of that understanding.

"Laws which subsist at the time and place of the making of a contract"—in this case the Credit Agreement between PREPA and the local banks—"enter into and form a part of it." *Norfolk & W. Ry. Co.* v. *Am. Train Dispatchers Ass'n*, 499 U.S. 117, 130 (1991). This principle has long been applied in the bankruptcy context: "It is inferred that insolven[cy] laws of the State in which any contract is made, form a part of the obligation of the contract." *Ogden* v. *Saunders*, 25 U.S. 213, 219 (1827).

When the local banks agreed to extend credit to PREPA, Puerto Rico had not enacted—*and was not permitted to enact*—bankruptcy legislation that would allow PREPA to dispense with its obligations without each creditor's consent. Instead, pursuant to its power under the Bankruptcy Clause of the Constitution, Congress had *precluded* Puerto Rico and the 50 states

from enacting municipal bankruptcy legislation, and it had also *precluded* Puerto Rico's municipalities from filing for protection under Chapter 9 of the Bankruptcy Code.

The Bankruptcy Clause provides that "The Congress shall have Power To . . . establish . . . uniform Laws on the subject of Bankruptcies throughout the United States. . . ." U.S. Const. Art. I, § 8, cl. 4. The Framers were mindful of the "wildly divergent schemes" that the States had implemented "for discharging debtors," *Cent. Va. Cmty. Coll.* v. *Katz*, 546 U.S. 356, 365 (2006), and they wanted to put an end to "private bankruptcy laws"—namely, non-uniform laws discharging particular debtors, *Ry. Labor Executives' Ass'n* v. *Gibbons*, 455 U.S. 457, 472 (1982).

Ever since 1946, Congress has exercised its power under the Bankruptcy Clause to prevent States, territories, and other U.S. possessions from enacting their own municipal bankruptcy schemes. *See* Act of July 1, 1946, ch. 532, § 83(i), 60 Stat. 409, 415 (1946). As set forth in Section 903(1) of the Bankruptcy Code, enacted in 1978: "[A] State law prescribing a method of composition of indebtedness of [a] municipality may *not* bind any creditor that does not consent to such composition." 11 U.S.C. § 903(1) (emphasis added).

In 1984, Congress expressly *included* Puerto Rico in the Bankruptcy Code's definition of "State," confirming that the Commonwealth is barred from enacting its own municipal bankruptcy legislation. 11 U.S.C. § 101(52).[21] At the same time, however, Congress *excluded* Puerto Rico from the definition of

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[21] Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98–353, § 421(j)(6), 98 Stat. 333, 368–39 (codified as amended at 11 U.S.C. § 101(52)).

State for the "purpose of defining who may be a debtor under chapter 9." *Id.* Thus, absent further Congressional action, Puerto Rico's municipalities are barred from seeking relief under Chapter 9 of the Bankruptcy Code. *Id.*

The Recovery Act, if upheld, would thus significantly alter the legal context in which the local banks agreed to extend credit to PREPA beginning in 2012. Despite Congress's determination to prevent Puerto Rico from "prescribing a method of composition of indebtedness" for municipalities, 11 U.S.C. § 903(1), the Recovery Act would empower PREPA to undertake a nonconsensual restructuring of its debt obligations. Specifically, under Chapter 2 of the Recovery Act, PREPA would be able to restructure its fuel line based on a vote of less than a majority of the local bank lenders.[22] And under Chapter 3, PREPA could restructure the fuel line even if all the local banks were to object, provided that *another* class of creditors supports the plan.[23]

The Recovery Act conflicts not only with Section 903(1) of the Bankruptcy Code, but also with the loan agreements negotiated against the backdrop of Section 903(1) and predecessor statutes. As discussed above, the Credit Agreement governing the fuel line is closely integrated with the Trust Agreement governing PREPA's bond debt: The Credit Agreement provides that all loans under the fuel line constitute "Current Expenses" (as defined in the Trust Agreement), which, under both the Trust Agreement

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[22] Recovery Act § 202(d) (restructuring requires participation of 50% of the amount of debt in a class, and 75% of the amount of participating debt).

[23] Recovery Act §§ 312, 315.

and the Credit Agreement, must be paid on a priority basis—even if it requires an increase in PREPA's electricity rates.[24]

The Trust Agreement, in turn, sets forth the specific remedies available if PREPA fails to meet its obligations, including by failing to pay all "Current Expenses." Section 804 of the Trust Agreement provides that, in the event of a default, the trustee has the authority to seek appointment of a receiver in accordance with the Puerto Rico Electric Power Authority Act.[25] That law, enacted in 1941, grants broad authority to a receiver to manage the affairs of PREPA by, among other things, increasing PREPA's revenues, cutting costs and collecting debts owed to PREPA.[26]

PREPA and its creditors thus expressly contemplated the possibility that PREPA would face financial distress. They agreed that a *receivership* would be the mechanism used to protect customers and creditors alike, based on long-standing Puerto Rico law defining the powers of a receiver.[27] The Recovery Act, by

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[24] Credit Agreement §§ 2.14, 5.09; Trust Agreement § 502.

[25] *See* Trust Agreement § 804; P.R. LAWS ANN. tit. 22 §§ 191 *et seq.*

[26] P.R. LAWS ANN. tit. 22 § 207(b), (e).

[27] In arguing that PREPA creditors understood that the Commonwealth could enact its own restructuring law, PREPA points to a boilerplate provision in the Trust Agreement defining an "event of default" to include, among other things, the institution of a proceeding by PREPA "for the purpose of adjusting the claims of . . . creditors pursuant to any federal or Commonwealth statute now or hereafter enacted." PREPA Br. at 19 n.12. This provision offers no support to PREPA's position. By definition, event of default provisions encompass acts by the borrower that the lenders do not believe are lawful or permitted:

authorizing PREPA to commence a bankruptcy proceeding in lieu of a *receivership*, would disrupt this agreement.

As economists have observed, a "municipality's eligibility to file for bankruptcy protection" is a "feature of its securities."[28] Accordingly, municipalities that are not eligible for bankruptcy protection—including municipalities in the many *states* that do not permit their municipalities to file for bankruptcy under Chapter 9 of the Bankruptcy Code[29]—receive favorable treatment in the credit markets.[30] When PREPA accessed the credit markets, it necessarily benefited from its legal status as a borrower that had not been made eligible to file for bankruptcy. The Recovery Act, if reinstated, would permit PREPA to retain that benefit while depriving PREPA's creditors of their end of the bargain, including the right to seek appointment of a receiver if necessary to address PREPA's financial problems.

For example, the Credit Agreement defines "event of default" to include, among other things, commencement of proceedings under "foreign" bankruptcy laws, claims by the borrower that the Loan Documents are invalid, or failure to comply with applicable law. Credit Agreement, Art. VII(h), (k), § 5.07.

[28] Tima T. Moldogaziev, et al., *Bankruptcy Risk Premium in the Municipal Securities Market*, 4, 14 (2014), *available at* http://cdn.bondbuyer.com/media/pdfs/BBrandeis14-Tima-paper.pdf.

[29] At present, 23 states either do not authorize or expressly prohibit their municipalities from filing for bankruptcy protection under Chapter 9. Of the remaining states, 15 place conditions or limitations on filings. *See id.* at 3.

[30] *Id.* at 4 (municipal bond issuers in states that authorize Chapter 9 filings incur a "bankruptcy risk premium").

II. THE RECOVERY ACT ILLUSTRATES WHY CONGRESS CHOSE TO PREEMPT STATE MUNICIPAL BANKRUPTCY LAWS.

By authorizing Congress to establish uniform bankruptcy laws, the Framers empowered Congress to preempt state-level bankruptcy legislation designed to protect "local interests" or the "temporary interests and popularity" of legislators. 3 Joseph Story, *Commentaries on the Constitution* § 1102 (1833), *in* 2 THE FOUNDERS' CONSTITUTION 640 (Philip B. Kurland & Ralph Lerner eds., 1987). Consistent with that idea, Congress enacted Section 903(1) of the Bankruptcy Code: Congress understood that state laws "prescribing a method of composition of indebtedness of [a] municipality" raise precisely the problems that the Framers wanted to avoid when they adopted the Bankruptcy Clause.[31]

The process used to enact the Recovery Act, as well as the substance of the Act, provide a case study showing why Congress insisted upon uniform federal law in the area of municipal bankruptcy. Puerto Rico passed the Recovery Act a mere three days after it was introduced, at the end of a legislative session, when

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[31] *See* S. REP. NO. 95-989, 110 (1978) (noting that section 903(1) was necessary to maintain the uniformity of the bankruptcy laws by preventing states from "enact[ing] their own versions of Chapter IX" (internal quotations omitted)). These same concerns led Congress to enact section 83(i) of the Bankruptcy Act, Chapter 9's predecessor statute. *See* H.R. REP. NO. 79-2246, 4 (1946) ("[A] bankruptcy law under which bondholders of a municipality are required to surrender or cancel their obligations should be uniform throughout the 48 states, as the bonds of almost every municipality are widely held. *Only under a Federal law should a creditor be forced to accept such an adjustment without his consent.*" (emphasis added)).

the Commonwealth's public corporations were already in financial distress.[32] Before enactment of the Recovery Act, there were no public hearings or other opportunities for public comment or debate.[33]

The Recovery Act's hasty passage, at a time when the would-be debtors under the Act were already in distress, could hardly contrast more with the process used by Congress to enact Chapter 9 and its precursor, Chapter 10 of the Bankruptcy Act. *See* Act of Aug. 16, 1937, ch. 657 §§ 81-82, 83(a), 50 Stat. 653 (1937). That process involved extensive review, public hearings, and comprehensive committee reports. *See United States* v. *Bekins*, 304 U.S. 27, 50-51 (1938) (describing Congress's "careful" consideration of potential objections to Chapter 10); *see also* 5 COLLIER ON BANKRUPTCY ¶ 81.01 (14th ed. 1978) (reviewing the legislative history of Chapter 9).

The substance of the Recovery Act reflects the flawed process by which it was enacted. As commentators have observed,[34] the Recovery Act diverges from

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[32] *Puerto Rico Bill Would Issue Debt to Repay $2 bln to GDB*, REUTERS (July 24, 2014), http://mobile.reuters.com/articleid USL2N0PZ2FH20140724 ("bill [was] quietly filed in late June near the end of the last legislative session with no public hearings").

[33] Reid Wilson, *Looming Puerto Rico Debt Deadlines Have Investors Nervous*, WASH. POST (July 24, 2014), https://www.washingtonpost.com/blogs/govbeat/wp/2014/07/24/looming-puerto-rico-debt-deadlines-have-investors-nervous/ ("'There was no time for comment, no hearings, no nothing,' said Arturo Porzecanski, director of the International Economic Relations Program at American University's School of International Service.").

[34] *See, e.g.*, Lorraine S. McGowen, *Puerto Rico Adopts a Debt Recovery Act for Its Public Corporations*, 10 PRATT'S J. BANKR. L. 453, 460–62 (2014).

federal bankruptcy law in critical ways that are unfavorable to creditors. For example:

- The Recovery Act allows the debtor to use the cash collateral of secured lenders without providing "adequate protection" against diminution of the collateral value. *Compare* Recovery Act § 207(a) (adequate protection discretionary), *with* 11 U.S.C. § 363(e) (adequate protection mandatory).
- The Recovery Act allows the debtor to obtain new credit subject to a senior lien—without providing adequate protection to the prior lien-holder—if "the proceeds are needed to perform public functions." *Compare* Recovery Act § 322(c), *with* 11 U.S.C. § 364(d) (requiring adequate protection to existing lienholder).
- Chapter 2 of the Recovery Act permits binding modifications to loan agreements, as part of a streamlined "consensual procedure," with the assent of creditors holding as little as 37.5% of the affected debt. *See* Recovery Act § 202(d) (allowing modification of debt with 75% support of participants representing at least 50% of the affected debt); *see Franklin Cal. Tax-Free Trust* v. *Puerto Rico*, 805 F.3d 322, 332 (1st Cir. 2015) ("There is no analogous 'consensual procedure' under federal law.").
- Chapter 3 of the Recovery Act permits "cram-down" of an entire class of creditors as long as another class of creditors supports the plan and the dissenting class is given the minimal amount it would receive in a liquidation on the petition date. *Compare* Recovery Act § 315(d), *with* 11 U.S.C. § 1129(b)(1) (requiring that plan be, among other things, "fair and equitable").

- The Recovery Act permits the Governor of Puerto Rico to institute an involuntary proceeding against a public corporation if the Government Development Bank (which is itself a creditor of certain public corporations) determines that doing so would be in the best interest of the entity and the Commonwealth. *See* Recovery Act §§ 201(b)(2), 301(a)(2).[35]

- All proceedings under the Act and disputes relating to the Act would occur in the Court of First Instance in San Juan, a Commonwealth court that does not specialize in complex debt restructurings. *See* Recovery Act §§ 102(18), 109.

The Recovery Act, in sum, highlights the problems presented by the kind of non-uniform, debtor-friendly "private bills" that Congress expressly preempted when it preserved for itself the exclusive power to enact municipal bankruptcy laws. If ever there were a law that, to borrow Justice Story's words, unduly protects "local" and "temporary" interests at the expense of broader and longer-term interests, the Recovery Act is it.

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[35] States are likely barred from instituting an involuntary proceeding on behalf of a municipality by section 109(c)(4) of the Bankruptcy Code, which requires that a potential municipal debtor "desire[] to effect a plan to adjust such debts." *See* Clayton P. Gillette, *Fiscal Federalism, Political Will, and Strategic Use of Municipal Bankruptcy*, 79 U. CHI. L. REV. 281, 297 (2012).

III. THE RECOVERY ACT IS NOT NECESSARY TO PREPA'S EFFORTS TO IMPROVE ITS OPERATIONS AND RESTRUCTURE ITS DEBTS.

Nor is the Recovery Act somehow necessary, as petitioners and their *amici* suggest, to enable an otherwise "helpless" Commonwealth to "address the crisis plaguing its municipalities." GDB Br. at 1, 31; Commonwealth Br. at 3. Without the Recovery Act, they claim, PREPA "could be compelled to ration its fuel supply" and employ "rolling blackouts" on the island, and it would be stuck in a "proverbial no man's land." PREPA Br. at 6; GDB Br. at 1.

These dire predictions are totally divorced from what has actually happened since the Recovery Act was declared invalid more than a year ago. During that period, PREPA and its creditors have been engaged in intense negotiations—which culminated in the RSA dated November 5, 2015. The RSA represents a crucial step forward: *First*, in exchange for the concessions of its creditors, PREPA has committed to take steps necessary to reform its operations and become a more efficient utility.[36] *Second*, the RSA includes a broad-based agreement by creditors to modify PREPA's financial obligations.

At the heart of the RSA is a robust program to improve PREPA's operations. Among other things, PREPA has agreed to implement new safety protocols; reform its billing and collection processes; work with Commonwealth agencies to set up payment plans for past-due government accounts; and institute a

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[36] *See* Krueger Report at 18 ("The silver lining in PREPA's financial difficulties is that it has forced the public enterprise to confront its problems of overstaffing and inefficiency.").

process to secure favorable pricing and credit terms on new supply contracts.[37] These reforms, when implemented, will create a more efficient utility, benefiting not only PREPA's creditors but also the people of Puerto Rico.

The RSA also provides for the consensual restructuring of PREPA's debt obligations. Under the RSA, which has the support of the vast majority of PREPA's creditors, bondholders have agreed to accept a 15% reduction of their claims, and both bondholders and the local banks have agreed to an extension of maturities.[38]

PREPA attempts to downplay the importance of the RSA—to which PREPA is itself a party—by asserting that the agreement is subject to contingencies, including termination events and holdout risks. PREPA Br. at 4-5. But most of the important contingencies fall within the control of Puerto Rico. In particular, Puerto Rico was required to enact legislation to implement the RSA. The Puerto Rico Energy Commission also must approve a new rate

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[37] *Exploring Energy Challenges and Opportunities Facing Puerto Rico: Oversight Hearing Before the H. Comm. on Nat. Res., Subcomm. on Energy and Mineral Res.*, 114th Cong. (Jan. 12, 2016) (statement of Lisa Donahue), *available at* http://www.aeepr.com/Docs/Lisa%20Donahue%20Testimony%20to%20Senate%20SubCommittee%20on%20Energy%20and%20Resources.pdf; *see also* PREPA Public Disclosure, Amended and Restated Restructuring Support Agreement, Schedule V (Dec. 24, 2015), *available at* http://emma.msrb.org/ES745050-ES584091-ES979961.pdf.

[38] *See* PREPA Public Disclosure, Amended and Restated Restructuring Support Agreement, Annex D (Dec. 24, 2015), *available at* http://emma.msrb.org/ES745050-ES584091-ES979961.pdf.

structure, and a Puerto Rico court must validate new securitization bonds.[39]

Nor is there any basis for PREPA's assertion that the Recovery Act somehow facilitated the negotiations that led to the RSA (PREPA Br. 11); to the contrary, the parties reached an agreement many months *after* the Recovery Act was struck down. *See* pp. 6-7, *supra*. What made the negotiations successful was not the invalidated Recovery Act, but rather an alignment of interests among PREPA's various stakeholders. PREPA's creditors do not have liens on PREPA's physical assets or a mechanism to secure recoveries if PREPA ceases operations. The creditors therefore have an overriding interest in making sure that PREPA continues to operate while at the same time becoming more efficient. The RSA, if effectuated, will achieve those goals on a consensual basis. The Recovery Act, in contrast, would put the parties' consensual agreement at risk and open the door to years of potential litigation in the context of a new and untested local bankruptcy regime.

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[39] *See id.*

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted,

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